Hasbro Second Quarter 2014
Financial Results Conference Call Management Remarks
July 21, 2014

Debbie Hancock, Hasbro, Vice President, Investor Relations:

Thank you and good morning everyone.

Joining me this morning are Brian Goldner, Hasbro's President and Chief Executive Officer, and Deb Thomas, Hasbro's Chief Financial Officer. Today, we will begin with Brian and Deb providing commentary on the company's quarterly performance and then we will take your questions.

Our second quarter earnings release was issued this morning and is available on our website. Additionally, presentation slides containing information covered in today's earnings release and call are also available on our site. The press release and presentation include information regarding Non-GAAP financial measures. Please note that whenever we discuss earnings per share or EPS, we are referring to earnings per diluted share.

Before we begin, I would like to remind you that during this call and the question and answer session that follows, members of Hasbro management may make forward-looking statements concerning management's expectations, goals, objectives and similar matters. These forward-looking statements may include comments concerning our product and entertainment plans, anticipated product performance, business opportunities, plans and strategies, costs and cost savings initiative, financial goals and expectations for our future financial performance.

There are many factors that could cause actual results or events to differ materially from the anticipated results or other expectations expressed in these forward-looking statements.

Some of those factors are set forth in our annual report on form 10-K, our most recent 10-Q, in today's press release and in our other public disclosures. You should review such factors together with any forward looking statements made on today’s call.

We undertake no obligation to update any forward-looking statements made today to reflect events or circumstances occurring after the date of this call.

I would now like to introduce Brian Goldner.

Brian Goldner, Hasbro President and CEO:

Thank you Debbie. Good morning everyone and thank you for joining us today.

Our second quarter performance reflects the ongoing global execution of our strategic brand blueprint as we transform Hasbro into the leading branded play company across consumers and geographies.

Every brand we develop - whether it is a Hasbro Franchise Brand, a new or existing Hasbro brand or one of our esteemed partners' brands - is being re-imagined across the blueprint to enable us to tell compelling stories globally. Our commitment to deliver the right content, with the right innovation, for the right audience in the right market is unwavering.

In the second quarter, Hasbro's revenues grew 8%. This growth was fueled by a 36% gain in Franchise Brands, 17% growth in the International markets - with Emerging markets up 30% - and 35% growth in Entertainment and Licensing - led by lifestyle licensing and digital gaming increases. Each one of these is a core element of our brand blueprint today and going forward.

Entertainment is supporting many of these brands – for example, TRANSFORMERS, MY LITTLE PONY, and Franchises under the MARVEL brand. Yet, not all growing brands are entertainment backed in the traditional sense, but they are leveraging tremendous stories to enthrall consumers around the world. Brands like PLAY-DOH and NERF, both up double-digits in the quarter, are examples of this strategy coming to life across the blueprint.

Just this week, storytelling and innovation are converging at Comic-Con International in San Diego. Fan driven Hasbro brands including MY LITTLE PONY, MAGIC: THE GATHERING, TRANSFORMERS and JEM AND THE HOLOGRAMS, a brand we are re-imagining through entertainment and licensing, are engaging with some of our most avid fans. We are unveiling exciting new initiatives which tap into creativity and engagement, including SuperFanArt.com, where we will leverage the creativity of fans with the technology of 3D printing - and you'll hear more about this in the near future.

As we look more closely at the quarter, it is clear that the Revolution in Geography that we have recently outlined for you is upon us. We grew our business double digits in all major international regions – Europe up 16%, Latin America up 17% and Asia Pacific also up 17%. Emerging markets including Russia, Brazil and China continue to contribute to the strong revenue gains in the segment, up 30% in the quarter.

I'd like to take a minute and congratulate the Latin American team on its 4th consecutive quarter of double-digit year-over-year growth. The team is doing a doing a tremendous job executing our brand blueprint to grow in a competitive market and a challenging retail environment.

In the U.S. and Canada segment, second quarter revenues were down 2%, but U.S. POS was up double digits for Toys, across the Girls, Boys and Preschool Toy categories, and was up double digits for Games. Our Franchise Brands POS at our top 5 retailers in the U.S. was up significantly in the quarter, led by NERF, MY LITTLE PONY, PLAY-DOH and TRANSFORMERS. In Canada, POS also increased across categories in Toys and Games. Clearly, there is momentum in our brands with U.S. and Canadian consumers.

Looking across the business, this momentum is evident globally. 5 of our 7 Franchise Brands grew revenue this past quarter, TRANSFORMERS, NERF, MY LITTLE PONY, MONOPOLY, and PLAY-DOH. Of the remaining Franchise Brands, MAGIC: THE GATHERING declined low single digits and is flat year-to-date, while LITTLEST PET SHOP has been re-imagined and an all new line hits shelves during the third quarter in markets around the world.

Franchise Brand TRANSFORMERS, along with gains in franchises under the MARVEL brand, helped deliver 32% revenue growth in the Boys category.

Transformers: Age of Extinction has been incredibly well received world-wide since its opening in late June. It has earned over $775 million globally, breaking records in many countries, including China, where the film is now the highest grossing film ever. Many international markets only recently launched following the conclusion of the FIFA World Cup, and as of this weekend it has opened in most major international territories.

Growth in Marvel in the quarter was driven by the Avengers Franchise, supported by the 2014 film *Marvel's Captain America: The Winter Soldier* and two animated series and the Spider-Man franchise, supported by *The Amazing Spider-Man 2* and the *Ultimate Spider-Man* animated series, combined with innovative new products such as MARVEL SUPER HERO MASHERS. *Marvel's Guardians of the Galaxy* will be in theatres on August 1 and the product is hitting retail in many markets at this time.

NERF revenues in the Boys category were down in the quarter, based on the timing of shipments, but are up year-to-date and POS is growing in several markets we track, including very strong growth in the U.S.

MY LITTLE PONY, MY LITTLE PONY EQUESTRIA GIRLS and NERF REBELLE contributed to growing the Girls category 10% in the quarter, more than offsetting the decline in FURBY. We have identified FURBY as a difficult comparison in 2014 and looking ahead that comparison does not get easier as the second half of last year represented more than 70% of 2013 FURBY revenues.

We have innovative new initiatives in the second half of this year including the launch of the re-imagined LITTLEST PET SHOP, MY LITTLE PONY POP, and all new MY LITTLE PONY EQUESTRIA GIRLS product and entertainment, building on the EQUESTRIA GIRLS position as the #5 Fashion Themed Doll property year to date in the U.S, according to NPD. In addition, PLAY-DOH DOHVINCI is just now on shelves and contributed slightly to the Girls category in the second quarter.

Moving to the Games business, despite positive POS in several markets including the U.S., UK, Germany and Canada, our Games revenues in the quarter declined 12%. There are several new games and market initiatives planned for the second half of this year, and we remain focused on growing the Games business for the long term across all platforms.

For the second quarter, Franchise Brand MONOPOLY continued to post positive growth with an all new MONOPOLY JR. in the market now and MY MONOPOLY coming for the fall. The category also benefitted from the addition of Backflip Studios revenues and growth in THE GAME OF LIFE as well as initial shipments of SIMON SWIPE.

This growth, however, was offset by declines in TWISTER, which had strong growth last year; DUEL MASTERS, a Japanese Trading Card game; and MAGIC: THE GATHERING which declined in the U.S. and Canada segment but grew in the International segment.

As we discussed before, MAGIC is release driven, and over the longer term, poised for growth as we continue to invest in the brand and technology development to enable global MAGIC players and new recruits to enjoy playing across digital and analog formats.

Last month, we released MAGIC: THE GATHERING—CONSPIRACY and that has led to increased casual-play activity in stores. In addition, fans are eagerly anticipating the release this month of the Magic 2015 Core Set which positions us well for the year.

Strategically, the second half of the year is extremely important for the Games category given the high consumer purchases over the holiday period. We have compelling new innovative games across consumer groups including MY MONOPOLY, SIMON SWIPE and BATTLE MASTERS featuring TRANSFORMERS - which is in market now – and will feature MARVEL properties this fall.

Finally, the Preschool category revenues declined 4%. PLAY-DOH continued to grow as did TRANSFORMERS RESCUE BOTS. This growth was more than offset by other declines in the category, including core PLAYSKOOL and SESAME STREET initiatives.

In closing, through the execution of our brand blueprint, we are creating compelling and engaging experiences for our consumers globally. Building on this, we are leveraging the financial strength of our business, which Deb will speak to, to invest in the transformation of Hasbro and execution of our blueprint to profitably grow Hasbro for the long term, in an environment of accelerating change. Our second quarter performance positions us well to successfully execute over the remainder of 2014 and in the coming years.

Now, I’d like to turn the call over to Deb.

Deb Thomas, Hasbro CFO

Thank you Brian and good morning everyone.

Our second quarter results reflect growth in key initiatives, including our Franchise Brands and Emerging Markets, while continuing to strategically invest in our brands, our systems and our capital structure. During the quarter, we successfully repaid $425 million of debt and raised a total of $600 million at the lowest coupon in our history. Heading into our peak working capital period, our cash position is strong and our inventories are well positioned for the holiday season.

Before we review our results, please note that in the second quarter 2014 we had an unfavorable tax adjustment of $13.8 million, or $0.10 per diluted share, related to a proposed resolution of outstanding tax matters. For the six months, nearly all of this adjustment will be offset by the favorable tax adjustments in the first quarter 2014. Absent any additional adjustments, we do not anticipate calling these items out in the full-year 2014 results.

Additionally, in 2013 we had pre-tax pension charges in SD&A of $2.5 million, or $0.01 per diluted share, related to partial pension settlement charges associated with restructuring actions. We have included a reconciliation to reported amounts in today's release. During the rest of my discussion of our business, I will exclude these items as they do not speak to the underlying performance of Hasbro.

Looking at our segments,

Second quarter revenues in the U.S. and Canada segment declined 2%. Both the Boys and Girls categories revenues grew in the quarter, but were offset by declines in the Games and Preschool categories. As Brian mentioned, U.S. POS trends were strong, increasing double digits at our top 5 retailers across all product categories. POS in Canada increased as well. We ended the quarter with inventory of good quality at retail and at Hasbro, and we are well positioned for the second half of the year.

Segment operating profit in the U.S. and Canada declined 20% in the quarter, primarily due to lower revenues and the impact of product mix. The Games category revenues declined including high margin trading card games DUEL MASTERS and MAGIC: THE GATHERING, which as Brian discussed, was impacted by the timing of releases year-over-year. Additionally, we are making incremental investments to support the long-term growth opportunity for MAGIC: THE GATHERING.

In the International segment, second quarter revenues increased 17% as all major regions grew double digits. Additionally, the Boys, Girls and Preschool categories all grew and more than offset a decline in the Games category.

The 17% revenue growth drove a 98% increase in operating profit as the International segment posted an operating profit of $29.2 million compared to $14.8 million last year.

Entertainment and Licensing segment revenues also delivered strong double-digit growth, increasing 35% in the second quarter. This growth was the result of higher lifestyle licensing revenues for Hasbro Franchise Brands, including MY LITTLE PONY, MONOPOLY and TRANSFORMERS, as well as growth in digital gaming and the addition of Backflip Studios.

Entertainment and Licensing segment operating profit increased nearly fourfold to $14.6 million compared to $3.7 million a year ago, driven by the impact of higher revenues and lower program production amortization.

Looking at our overall expenses, our business reflects the long-term investments we are making in re-imagining our brands and executing across the brand blueprint globally. At the same time, we are lowering our overall cost basis to achieve our goal of $100 million in underlying cost savings by 2015.

Cost of sales as a percentage of revenue in the quarter declined. This decline reflects growth in entertainment properties, including TRANSFORMERS and MARVEL properties, as well as higher Entertainment and Licensing revenues.

The higher entertainment backed revenues also resulted in higher royalty expense in the quarter, which increased to 8.5% of quarterly revenues. As we outlined in February, over the past five years our average royalty rate has been around 7.3%. We expect full year 2014 royalties to be at or slightly above that five year average.

Product development as a percent of revenues was flat year-over-year even with the addition of Backflip Studios, which we acquired in the third quarter of 2013, and continued incremental investments in MAGIC: THE GATHERING. Absent these items, product development dollars would have been consistent with a year ago, reflecting our expected cost savings.

Intangible amortization declined slightly as some of our assets have become fully amortized. This was partially offset by incremental expense associated with Backflip Studios.

Program production cost amortization declined year-over-year and advertising increased slightly, as we invest in building awareness and demand for our brands.

SD&A declined as a percentage of quarterly revenues reflecting the impact of higher revenues in addition to lower underlying costs in the business and the positive results of our ongoing cost savings initiative. These declines were impacted by the factors we spoke to in February, including higher compensation and investments into long-term growth opportunities including Backflip and MAGIC: THE GATHERING.

Turning to our results below operating profit for the quarter:

Other income was $4.8 million versus other expense of $800,000 in 2013. Our 50% share in the Hub Network improved to a profit of $2.3 million versus $131,000 last year.

Additionally, we benefited from lower foreign exchange losses and improved investment returns in 2014.

The second quarter underlying tax rate declined to 26.8% versus 27.3% in the second quarter 2013, and we continue to expect our full-year underlying tax rate to be in the range of 26 to 27%.

For the quarter, average diluted shares were 130.9 million shares compared to 132.0 million in 2013, reflecting our active stock repurchase program. The actual amount of shares outstanding at the end of the second quarter 2014 was 127.9 million.

Diluted earnings per share, absent charges, in the second quarter 2014 were $0.36 versus $0.29 in 2013.

At quarter end, cash totaled $586.2 million. Our cash position is strong and we continue to prioritize investing back into Hasbro for the long-term profitable growth of the business. We are returning cash to our shareholders in the form of dividends and share repurchases and as we stated earlier this year, this level of activity is higher than last year. Finally, we remain committed to executing against these priorities in a manner consistent with maintaining our solid investment grade rating.

In the second quarter, we returned $192.0 million to shareholders: $55.7 million in cash dividends and $136.3 million in share repurchases. At quarter-end, $308.1 million remained available in our current share repurchase authorization. In the first six months of the year, we have repurchased 4 million shares, returning $216.8 million to shareholders.

During the second quarter, we closed a $600 million notes offering and paid down $425 million of long-term debt which came due in May. The deal was very well received by the market and enabled us to achieve the lowest coupon in Hasbro's history.

Receivables at quarter end increased 15% versus 2013. DSOs were 80 days compared to 75 days in 2013. The Revolution in Geography which Brian spoke of also means a higher percentage of our sales are in international and emerging markets where DSO payment terms are generally longer. This revenue mix is resulting in higher DSOs for Hasbro overall. Additionally, in the second quarter, the timing of collections and shipments also contributed to the growth in DSOs.

Inventories increased $132.8 million versus last year with approximately two-thirds of the increase coming from international markets. Our inventory at U.S. retail was down again this quarter and of good quality, and internationally our inventory at retail is healthy. Overall, retail and Hasbro-owned inventory is of good quality and we believe we are well positioned for the important second half of the year with the right inventory in the right markets.

In closing, while the all-important second half of the year is still ahead of us, we are pleased with our second quarter results. They reflect the investments we have been making in our brand blueprint, the innovation in our storytelling, product lines and licensing programs, and savings we expected at this stage of our cost savings initiative. They also reflect our commitment to our strategy and the investments we continue to make for the long-term success of Hasbro and our shareholders.

Brian and I are now happy to take your questions.